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July 9, 2007

TO: Supervisor Zev Yaroslavsky, Chairman
             Supervisor Gloria Molina
             Supervisor Yvonne B. Burke
             Supervisor Don Knabe
             Supervisor Michael D. Antonovich

FROM: J. Tyler McCauley
             Auditor-Controller

SUBJECT: **REVIEW OF WORKERS' COMPENSATION PAYMENT PROCESS**

At the request of the then Chief Administrative Office (CAO), we evaluated the program and internal controls utilized by the Department's Risk Management Branch (RMB) workers' compensation program. Our review was intended to ensure the CAO is appropriately monitoring the County's Third-Party Administrators (TPAs) and Medical Management Companies (MMCs) for compliance with established requirements for processing workers' compensation claims and resultant payments, and that the CAO has appropriate controls over the workers' compensation payment process.

As part of our audit, we reviewed the internal controls over the use of the GENCOMP computer system that is used to process workers' compensation payments and maintain workers' compensation data. Finally, we specifically analyzed why large numbers of workers' compensation payments are being returned by the Post Office as undeliverable.

Background

The CAO is responsible for administering contracts with TPAs and MMCs that process workers' compensation claims and resultant payments to service providers (e.g., doctors, labs, physical therapists, etc.) for injured County employees. In fiscal year 2005-06, the CAO issued through eCAPS approximately 350,000 workers' compensation payments, totaling approximately $263 million.

"To Enrich Lives Through Effective And Caring Service"

Summary of Findings

Our review disclosed significant issues with the internal controls over workers' compensation payments, and that TPA and MMC staff were not always complying with established procedures.

1. The vendor information on the GENCOMP system has not been reconciled to the information on eCAPS, the County's financial accounting and disbursement system. This has resulted in payments being returned as undeliverable by the Post Office, the CAO being unable to comply with eCAPS controls, and an excessive number of payments being made using the Miscellaneous Vendor Code.

2. Some TPA staff are not always complying with established payment approval procedures. Some agency staff are splitting some payments to avoid second approval requirements. This lack of compliance is also exposing the workers' compensation program to the risk of inaccurate, inappropriate, and potentially fraudulent payments.

3. Our computer assisted search of workers' compensation payments disclosed duplicate payments generated due to GENCOMP/eCAPS interface problems.

4. The interface between GENCOMP/eCAPS and internal controls over the GENCOMP system need to be improved to limit the risk of inappropriate, inaccurate, and potentially fraudulent payments.

It should be noted that we did not find evidence of fraudulent activity in the specific payments examined during our audit. However, due to issues of non-compliance with established procedures and the significant issues related to internal controls over the workers' compensation payment process, the Auditor-Controller's Office of County Investigations is conducting additional analytical procedures to determine whether any fraudulent payments have been issued.

It should also be noted that Auditor-Controller (A-C) and CAO staff have been working together to ensure the CAO complies with eCAPS procedures and controls, minimizes payment delays, and reduces the number of undeliverable payments. Beginning June 2007, CAO and A-C staff began meeting weekly to refine the automated matching procedures between GENCOMP and eCAPS. In addition, CAO staff plan to work with A-C staff to submit a weekly file to update the eCAPS vendor table.

In addition, the CAO needs to take further action to ensure TPA and MMC staff comply with all established procedures, and enforce existing internal controls and/or implement additional internal controls over its workers' compensation payment process. We have made specific recommendations to achieve these goals and achieve compliance with established procedures and internal controls for the payment process. Upon being

advised of the existence of some of the internal control weaknesses discussed in this report, the CAO proactively issued a memo to its TPAs reiterating certain established policies, establishing changes to existing procedures, etc.

We will continue to work closely with the CAO to ensure TPAs and MMCs comply with established procedures and that recommended additional internal controls are implemented on a priority basis. We plan to conduct a follow-up review within twelve months to assess the CAO's progress in implementing the recommendations in this report. Our follow-up will include reviewing the CAO's implementation of the new web-based version of GENCOMP, which occurred in March 2007, to ensure the new system provides appropriate controls over workers' compensation payments and data consistent with established procedures for TPAs and MMCs and payment security and internal controls discussed in this report.

Acknowledgement

Details of the results of our review are included in the attached report. We met with CAO management to discuss the results of our review. Their response, attached, indicates general agreement with our findings and recommendations. We thank CAO staff and management for their cooperation during our review.

Please call if you have any questions, or your staff may contact Jim Schneiderman at (626) 293-1101.

Attachment

JTM:MMO:JLS

c: David E. Janssen, Chief Executive Officer
   Rocky Armfield, Assistant Administrative Officer
   Sachi A. Hamai, Executive Officer
   Public Information Office
   Audit Committee

Chief Administrative Office
Risk Management Branch
Review of the Workers' Compensation Program

Background

The Chief Administrative Office (CAO) Risk Management Branch (RMB) is responsible for processing workers' compensation payments to injured employees and related service providers (e.g., doctors, labs, physical therapists, etc.). The CAO contracts with three Third-Party Administrators (TPAs) and three Medical Management Companies (MMCs) to perform workers' compensation claims evaluation and administers workers' compensation payments. In fiscal year 2005-06, the County issued approximately 350,000 workers' compensation payments, totaling approximately $263 million.

The TPAs receive claims/invoices from employees and service providers for review and approval by a claims adjuster. The claims adjusters review the case file and information on GENCOMP to ensure the services are consistent with the worker's injury and approve payments, stamping invoices that are approved. Most payments to injured workers are initiated and approved only by TPAs. Service provider invoices are sent to the MMCs, who determine the amount the County should pay based on the appropriate fee schedule. The TPAs and MMCs process the claims/invoices using the RMB's GENCOMP system. After approval, the TPAs use GENCOMP to submit the claims/invoices to RMB for payment through the County's eCAPS financial accounting system. RMB's role is to provide on-site monitoring of the claims services of each TPA and to ensure the payment of claims to employees injured on the job.

Scope of Review

We evaluated the program and internal controls utilized by the CAO workers' compensation program to ensure RMB is appropriately monitoring the TPAs and MMCs for compliance with established procedures for processing workers' compensation claims and payments, and that the CAO employs appropriate controls over the workers' compensation payment process.

As part of our audit, we performed a review of the internal controls over the use of the GENCOMP computer system that is used to maintain workers' compensation case data and to process workers' compensation payments. Finally, we specifically analyzed why large numbers of workers' compensation payments are being returned by the Post Office as undeliverable.

Workers' Compensation Payments

Undeliverable Payments

We tested a sample of 35 payments to service providers to determine why they were sent to an undeliverable address. Our review disclosed that 28 of the payments (80%) were sent to an undeliverable address because the payment file the CAO sent by

computer interface to eCAPS for payment did not match the vendor codes (including Taxpayer Identification Numbers (TINs)) and/or addresses on eCAPS. These mismatches are caused primarily by vendor information on GENCOMP not being successfully updated to the eCAPS vendor table. Mismatches also occur when there are discrepancies in the address information such as the use of "Street" on the vendor table of one system and "St." on the vendor information on the other system.

When the vendor information on the CAO's payment file does not match the information on eCAPS, the GENCOMP system instructs eCAPS to send the payment to an alternate address. In most of the instances where this occurred, the payment was mailed to an alternate address that had not been used on GENCOMP in some time, indicating it was an old address. For example, one of the payments was mailed to an address that had not been used on GENCOMP since August 1996. In addition, three of the 35 undeliverable payments (8%) had no documentation on file indicating the address to which the payments should be mailed.

As discussed in the Miscellaneous Vendor Payments section of this report, in February 2006, a programming change was made so that if the address and/or TIN on GENCOMP and the eCAPS vendor table do not match exactly, the payment is placed on "hold". This delay is intended to allow the CAO to correct the mismatches. If the CAO does not correct the mismatches within 30 days, the payments will be issued using a Miscellaneous Vendor Code to meet legal timeframes for workers' compensation payments.

The mismatch of information between GENCOMP and eCAPS, and the practice of adding or modifying vendor records in GENCOMP without validating the vendor information discussed later in this report, are significant internal control and computer interface weaknesses. These internal control issues and recommendations for improving internal controls are discussed in detail in the TPA Payment Controls section of this report.

Over the last two years, Auditor-Controller (A-C) eCAPS and CAO personnel have been working together to ensure the CAO complies with eCAPS procedures and controls, minimize payment delays, and reduce the number of undeliverable address payments. While some progress has been made, we believe that the CAO, in collaboration with A-C personnel, needs to implement the recommendations in this report to further reduce the number of undeliverable and Miscellaneous Vendor Code payments.

To prevent these mismatches and reduce the number of undeliverable payments, the CAO should continue to work with A-C eCAPS personnel to reconcile the vendor information (addresses and TINs) on GENCOMP to the information on eCAPS. This could be done by adding the GENCOMP vendor number to the vendor record in the eCAPS vendor table. This would ensure payments are sent to the GENCOMP mailing address. CAO and eCAPS staff should also ensure that the address files are reconciled on an ongoing basis to ensure payments are sent to the vendors' correct addresses.

Recommendations

CAO management:

1. **Continue to work with Auditor-Controller eCAPS personnel and complete a reconciliation of vendor information between GENCOMP and eCAPS.**

2. **Perform an automated reconciliation of the information on GENCOMP with the eCAPS vendor file on a bimonthly basis.**

3. **Continue to work with the Auditor-Controller to develop a method to ensure mismatches are corrected, and the information on GENCOMP and the eCAPS vendor tables are current and accurate so that payments are sent to the appropriate vendors' correct addresses.**

We did confirm that the 35 undeliverable payments we sampled were for open workers' compensation cases. Based upon our review, it appears the 35 payments were appropriate. We are performing additional analytical procedures to determine whether any fraudulent payments have been issued.

Use of Miscellaneous Vendors Codes for Payments to Vendors

The GENCOMP interface with the eCAPS vendor table information attempts to match the vendor address and TIN. In February 2006, at the direction of the A-C, the system was modified so that if the address/TIN on GENCOMP and the eCAPS vendor table do not match exactly, the payment is placed on "hold". If the mismatch is not corrected within 30 days, the payments are issued using a Miscellaneous Vendor Code to meet legal timeframes for workers' compensation payments.

The County Fiscal Manual (CFM) requires that Miscellaneous Vendor Codes only be used for one-time payments to vendors. Assigned vendor codes are required to be used whenever possible. Using assigned vendor codes ensures payments are made to validated vendors, increases the accuracy of vendor payments reported to taxing authorities, and ensures that management has accurate information on how much business vendors do with the County.

Between July 2005 and March 2006, the CAO issued 13,555 vendor payments using Miscellaneous Vendor Codes. However, 12,489 of these payments (92%), totaling $6 million, were not one-time payments to the vendors. CAO staff indicated that they made the payments using Miscellaneous Vendor Codes because the vendors were not on the eCAPS vendor table, or because the vendor was on the eCAPS table, but the GENCOMP address did not match the eCAPS address, and the payments had to be made within legally required timeframes.

Reconciling the GENCOMP vendor information to the eCAPS vendor table, as previously discussed, should significantly reduce the number of Miscellaneous Vendor Code transactions. Nevertheless, CAO management needs to continue working together with the A-C to take additional measures to ensure they comply with the requirement to only use Miscellaneous Vendor Codes for one-time payments by using automated procedures to detect vendors receiving multiple payments and add/update approved, verified vendor information to minimize use of the Miscellaneous Vendor Code. CAO staff, working together with the A-C, should also review payments in the hold file to correct mismatched addresses and add/update approved vendors to the eCAPS vendor file on a continuous basis.

Recommendations

CAO management:

4. **Use automated procedures to detect vendors receiving payments under Miscellaneous Vendor Codes and add/update approved vendors to minimize use of the Miscellaneous Vendor Codes.**

5. **Review payments in the hold file to correct mismatched addresses and add/update approved vendors to the eCAPS vendor file on a continuous basis.**

Controls Over the GENCOMP Vendor Table

We noted that the CAO adds vendors to the GENCOMP vendor table based on requests from the TPAs and MMCs without first validating the information (name, address, TIN). We also reviewed the GENCOMP vendor table and noted 2,462 duplicate vendor records (4% of the total records), and an additional 2,787 vendor records (4% of the total records) with missing information (street address, state, zip code, TIN, etc.).

The CAO with assistance from the Auditor-Controller should develop and implement strict, redundant controls for adding vendors to GENCOMP, modeling the controls used by the Auditor-Controller to add vendors to the eCAPS vendor table and verify that vendors' addresses exist. Specifically, TINs should be compared to Internal Revenue Service (IRS) records. Computer address validation software should be used to verify that the addresses exist. The CAO should also use other automated procedures to periodically review the GENCOMP vendor table, eliminate duplicate records and identify incomplete records for corrective action.

We also noted that the CAO does not delete or deactivate known bad addresses in GENCOMP. CAO staff indicated that this information is part of the vendor payment history and must be retained. If these addresses must be maintained on the system, the CAO must implement strict controls to deactivate and secure the known bad

addresses in GENCOMP to prevent them from being used and deactivate the bad addresses in the eCAPS vendor table.

Recommendations

CAO management with assistance from the Auditor-Controller:

6. **Develop and implement strict, redundant controls for adding vendors to GENCOMP modeling the controls used by the A-C to add vendors to the eCAPS vendor table, including comparing TINs to IRS records and using address validation software to verify that the addresses exist.**

7. **Use automated procedures to review the GENCOMP vendor table to eliminate duplicate records and identify incomplete records for corrective action.**

8. **Implement strict controls to deactivate and secure known bad addresses in GENCOMP to prevent them from being used, and deactivate the bad addresses in the eCAPS vendor table.**

TPA Payment Controls

As previously noted, TPAs initiate workers' compensation payments on behalf of the County. When a TPA receives a medical service invoice, a claims adjuster reviews the case file and information on GENCOMP to ensure the services are consistent with the worker's injury. TPA staff stamp the invoices indicating they have been approved. The TPA then sends medical service invoices to the MMCs to compute the amount that should be paid based on the fee schedules. The MMCs then send an Explanation of Review to the TPA and post the approved payment amount on the GENCOMP system.

When an MMC determines the amount to be paid to a service provider, a clerk at the TPA applies an on-line approval code on GENCOMP to release the payment. Payments under $4,000 require one approval at the TPA. Payments over $4,000 require a second approval. GENCOMP sends a payment file to eCAPS each night, and the eCAPS system issues the checks. Payments to injured workers (as opposed to services providers) are processed by the TPAs on GENCOMP without being reviewed by the MMCs, and a file is sent to eCAPS and the checks are then issued through eCAPS.

Our analysis indicated that approximately 11,780 payments of the 335,150 worker's compensation payments issued between July 2005 and March 2006 were potential duplicate or split payments.

We reviewed a selected sample of 125 of these potential duplicate or split payments. Our review indicates that, for some payments, some TPA staff were intentionally not always complying with established payment approval procedures, and some payments

we reviewed exceeded the supporting documentation in the workers' compensation case files. Specifically:

- The TPAs approved 2 payments, totaling $4,032, to an injured employee's caretaker after the injured employee died.

- Seven payments (6%) were made with no documentation that the invoices had been approved by TPA/MMC staff. The CAO has indicated that they located supporting documentation for these payments approximately one year after our review.

- Three payments (3%) over $4,000 at one TPA, the required second approval had been delegated by a Manager to a lower level supervisor.

- One invoice (1%) was processed by an MMC without the required TPA approval.

- Ten payments (8%) appeared to have been split payments. Some TPA staff acknowledged that they sometimes split payments to circumvent the requirement for a second approval on invoices over $4,000. TPA management also acknowledged that they were aware that payments are split.

In addition to our sample tests, we identified five payments, totaling $2,765 that were returned by the payees because they believed they were overpayments. In all five instances, we verified that the returned payment was an overpayment. These overpayments occurred because the TPA staff manually overrode the GENCOMP system control that suspends potential duplicate payments.

Our audit procedures indicate that some TPA and MMC staff are not always complying with the established workers' compensation payment approval procedures, sometimes intentionally. This failure to comply is resulting in the inappropriate payments noted in our payment analyses and could result in improper or fraudulent workers' compensation payments.

The CAO has monitoring staff assigned to each TPA. However, these monitors only review payments over $7,500. In addition, the CAO monitors review the TPAs' work. However, this monitoring focuses primarily on program issues (reasonableness of services, injury-related services, etc.). The CAO indicated that they do monitor TPA payment approvals and do require TPAs to reimburse the County for inappropriate payments.

The CAO needs to take immediate action to increase its monitoring of TPAs and MMCs to ensure they comply with established payment controls. We did verify that the sampled payments were made on valid workers' compensation cases. As noted earlier, we did not find evidence of fraudulent activity for the specific payments examined during our audit. However, we are conducting additional analytical procedures to attempt to determine whether any fraudulent payments have been issued.

Recommendation

9. **CAO management take action to increase its monitoring of TPAs and MMCs to ensure they comply with established payment control requirements.**

    Status Update: The CAO issued a memo to its TPAs in January 2007 reiterating the policy regarding Payment Authorization Requests, Split Payments and Delegation of Authority.

Secondary Approval Threshold

Payments of less than $4,000 only require one approval by the TPAs, and County monitors assigned to the TPAs only approve payments over $7,500. As a result, 99% of all workers' compensation and service provider payment transactions, or 76% of total workers' compensation dollars, are for payments with only one TPA approval at the time payments are made. CAO staff do validate the total amount paid to injured employees after-the-fact, when a case is resolved.

Based on the low percentage of payments that receive a second approval at the time the payments are made, CAO management should evaluate the feasibility of lowering the thresholds for requiring a second approval and for requiring County monitor approvals.

The review and approval of payments by the TPA adjustor and any subsequent required approvals were not recorded electronically on GENCOMP. These approvals are only recorded on hard copy documents contained in the case file. As previously discussed, the CAO implemented a new web-based version of GENCOMP in March of 2007. The CAO indicated that the updated system includes recording electronic approvals on GENCOMP.

Recommendation

10. **CAO management evaluate the feasibility of lowering the threshold dollar amount so that more payments require a second approval and for requiring County monitor approvals.**

     Status Update: The CAO issued a memo to its TPAs in January 2007 requiring the establishment of Random Payment Audits, which the CAO contends will produce the same outcome as the action described in Recommendation 10.

Separation of Duties

Proper internal controls require that the functions of creating an account and authorizing payments be separated. In addition, changes to the payee on an account or the

payee's mailing address should be made by staff independent of staff that create accounts and approve payments.

There are serious internal control weaknesses in these payment processing procedures, both to payments to service provider vendors and to injured employees. We noted that some TPA staff that enter cases on GENCOMP can also enter payments on those cases, approve the payments and change payment information. We also noted that TPA data entry staff can also change payee information, such as mailing addresses.

CAO management needs to take immediate action to ensure that TPAs implement internal controls that will maintain proper separation of duties related to creating cases, authorizing payments, entering payment approvals and changing payment information, such as address changes for service providers and injured workers. As previously . noted, we are performing additional audit procedures to determine if these payment processing weaknesses resulted in any incorrect or fraudulent payments.

Recommendations

CAO management:

11. **Take immediate action to ensure that TPAs implement and maintain proper separation of duties and controls related to creating cases, authorizing payments, entering payment approvals and changing payment information, such as address changes for service providers and injured workers.**

    Status Update: The CAO issued a memo to its TPAs in January 2007 describing certain changes in the payment request input process that will bring about improved separation of duties.

12. **Immediately increase its monitoring of the TPAs' separation of duties to ensure the prescribed internal controls remain in force.**

Controls at CAO

We evaluated the system controls, separation of duties and payment monitoring at the CAO, including GENCOMP system administration duties, payment monitoring activities, and exception and monitoring reports. We also reviewed the CAO's monitoring of the TPAs, returned warrant tracking, and the actions the CAO and the TPAs take to address overpayments.

System-Generated Duplicate Payments

Automated systems should include controls to prevent duplicate payments from occurring. These controls should include unique transaction and/or batch numbers that can only be processed once.

Our review indicates that the GENCOMP/eCAPs interface does not prevent duplicate payments. We analyzed workers' compensation payments from July 2005 to March 2006, and identified what appeared to be 536 duplicate payments totaling $242,022. We tested eight pairs of these payments and confirmed that the payments were duplicate payments. The total of the duplicates was $37,291.

Because of a lack of system documentation, we could not determine why the duplicate payments occurred. We discussed our findings with the CAO staff person responsible for the GENCOMP system. This individual indicated that he was aware of this problem and said it was due to a problem with the payment processing program. CAO staff asserted that corrective action has been taken to stop issuances of system-generated duplicate payments. However, we identified additional duplicates after March 2006, which indicates that the problem continued.

CAO management needs to continue to identify and recover all duplicate payments caused by the GENCOMP/eCAPS interface problems. The CAO also needs to identify and correct the program errors that create these duplicate payments and develop and maintain documentation of the interface.

Recommendations

CAO management:

13. **Work with A-C staff to identify all duplicate payments caused by GENCOMP/eCAPs interface and take steps to recover the overpayments.**

14. **Identify and correct the GENCOMP/eCAPs interface system program errors that allow duplicate payments to be created.**

15. **Develop and maintain documentation for the GENCOMP/eCAPS interface.**

Workers' Compensation Data Security

We noted that one CAO employee used an unsecured, unencrypted portable hard drive to store confidential data, such as vendor/employee names, Social Security/Taxpayer Identification Numbers (SSN/TIN), and addresses. The employee indicated that the drive was used to back up data files and for off-site access to workers' compensation data. We found no operational need for such off-site access.

Storing confidential data on an unsecured drive creates a serious risk of unauthorized access, loss, or theft of data generally, and specifically confidential data. This practice also violates the recently approved Chief Information Office policy on data security. If staff needs off-site access to workers' compensation data, management must establish controls to protect the data using a secure connection, such as a Virtual Private Network (VPN). Back-ups of workers' compensation data should only be maintained in a secure, locked location with access restricted to authorized individuals. We were advised by CAO staff that effective April 2006, the portable hard drive was no longer being used.

We also noted that this same person is assigned as the GENCOMP system administrator, programmer, database administrator, and is responsible for transmitting payment transactions to eCAPS. This lack of separation of duties could result in unauthorized transactions and system changes that could lead to inappropriate or fraudulent payments.

The CAO needs to ensure that a proper segregation of duties is maintained between the system administrator, programmer, database administrator, and payment processor functions to reduce the risk of unauthorized transactions and system changes.

Finally, we noted that CAO management does not have written policies to safeguard workers' compensation data.

Recommendations

CAO management:

16. **Ensure that workers' compensation data is not backed-up on an unsecured, unencrypted hard drive, and limit off-site access, if necessary, to a secure connection, such as VPN.**

    Status Update: As previously indicated, the CAO advised us that effective April 2006, the practice of using a portable hard drive to back-up workers' compensation data was discontinued.

17. **Separate the duties of system administrator, programmer, database administrator, and payment processor.**

18. **Develop written policies to safeguard workers' compensation data.**

GENCOMP Access Controls

Access controls are intended to ensure that only authorized staff can access a system. Chapter 7 of the County Fiscal Manual establishes the minimum control requirements to

reduce the risk of unauthorized system access. We noted that the CAO's controls over GENCOMP do not meet these requirements. Specifically:

- GENCOMP does not lock a user account after a number of failed log-on attempts. There is no limit to how many times a user may attempt to gain access. The system also does not log user access attempts. Logging access attempts is important because it allows management to identify potential security issues.

- User passwords do not expire. Passwords should be set to expire at least every 90 days.

- GENCOMP allows user passwords to be between three and sixteen characters long. The County's standard requires passwords have at least six characters.

- GENCOMP does not have an internal log of previously issued passwords, which when prompted for a password change, would require individuals to request new, not previously used, passwords.

- GENCOMP does not deactivate users who have not logged-on within a certain time period.

- GENCOMP does not automatically terminate user sessions after a specified period of inactivity. We noted that GENCOMP users often leave their terminals unattended when logged on. While access to various functions in the system is controlled by passwords, given the sensitive nature of the data, RMB should require staff to sign off or lock their terminals when they leave their desks.

- The CAO does not periodically review user access.

- Some GENCOMP user IDs are tied to a job duty and not to specific users. For example, multiple employees can log on as "Exam1", and the system will not be able to identify the specific employee who processes transactions under that ID.

The CAO implemented a new web-based version of GENCOMP in March 2007, and has indicated that this new version addresses several of the weaknesses discussed above.

Recommendation

19. **CAO management modify GENCOMP automated access controls to address the weaknesses noted in our review.**

   Status Update: The CAO issued a memo to its TPAs in January 2007 reiterating the policy regarding System Timeouts and Logouts.

Processing Controls

IT system processing controls are used to ensure a system is functioning properly, including accuracy, completeness, and timeliness. These controls include batch totals, error reports and procedures on evaluating processing results and reports.

The CAO needs to enhance its processing controls as follows:

- Develop monitoring reports for GENCOMP processing. The CAO needs to develop and prepare monitoring reports to ensure that files are updated completely and accurately and that unauthorized activities do not occur.

- Develop written procedures on how to review processing results to verify that processing was performed correctly. Examples of these types of controls would include reconciliation of batch totals, before and after processing, to ensure all transactions were processed, including procedures on recovery and to restart the system in the event of processing failures.

- Evaluate the feasibility of modifying GENCOMP to enable management to determine what transactions and activity were processed and to track changes made to individual transactions.

- Evaluate the feasibility of incorporating edits such as limits on the amounts and number of payments a payee can receive in a specified period to reduce the risk of improper processing. No such edits currently exist on GENCOMP.

Recommendations

CAO management:

20. **Develop monitoring reports to ensure that files are updated completely and accurately and that unauthorized activities do not occur.**

21. **Develop written processing procedures for GENCOMP on how to review processing results to verify that processing was performed correctly.**

22. **Evaluate the feasibility of modifying GENCOMP to enable management to determine what transactions and activity were processed and to track changes made to individual transactions.**

23. **Evaluate the feasibility of incorporating edits, such as limits on the amounts and number of payments a payee can receive in a specified period, to reduce the risk of inappropriate transactions.**

Change Controls /Business Continuity Plan

The County Fiscal Manual (CFM) requires departments to have controls over how changes to computer systems should be tested, approved and documented. Change controls are intended to reduce the risk of unauthorized changes and ensure that all changes are properly tested and approved by management. The CAO does not have formal controls over changes to its computer applications.

The CFM also requires departments to develop and periodically test a Business Continuity Plan (Plan) for all mission-critical systems to ensure operations could continue in the event of disasters, such as earthquake, fire, sabotage, etc. The CAO has not developed a Business Continuity Plan for the GENCOMP system.

Recommendations

CAO management:

24. **Develop and implement a formal change control policy for its computer applications.**

25. **Develop and test a Business Continuity Plan for GENCOMP.**

Internal Control Certification Program

County Code Section 2.10.015 requires County departments to evaluate their fiscal internal controls annually using the Internal Control Certification Program (ICCP) procedures provided by the Auditor-Controller. The ICCP is a self-assessment tool intended to allow departments to assess their own internal controls and take corrective action to ensure compliance with County policies and standards.

When the CAO last evaluated its computer controls in 2005 using the ICCP, they certified some controls were in effect when they were not. Many of the internal control weaknesses discussed in this report could have been identified if the CAO had completed the ICCP correctly. In addition, the ICCP requires that compliance with the controls be verified by someone independent of the function being reviewed. We noted that the ICCP for GENCOMP was completed by the system administrator. The CAO needs to ensure that the ICCP for GENCOMP is completed accurately and by someone independent of the system operations/administration.

In 1996, we approved the CAO's request to conduct ICCP reviews biennially. However, based on the internal control weaknesses identified in our review, we will require the CAO to complete the ICCP reviews for the GENCOMP system annually.

Recommendation

26. **CAO management ensure that the annual ICCP review of the GENCOMP system is conducted accurately and by someone independent of the system operations/administration.**

DAVID E. JANSSEN
Chief Executive Officer

July 9, 2007

To: J. Tyler McCauley
            Auditor-Controller

From: David E. Janssen
            Chief Executive Officer

AUDITOR-CONTROLLER'S REVIEW OF WORKERS' COMPENSATION PAYMENT PROCESS

The Chief Executive Office (CEO) reviewed the Department of Auditor-Controller's (A-C) *Review of Workers' Compensation Payment Process* and provides the following response. As you are aware, the CEO requested the A-C's review to enhance the effectiveness of the County of Los Angeles' (County) workers' compensation program; facilitate the interface between eCAPS and GenComp, the County's workers' compensation computer system; and to strengthen the CEO's fiscal monitoring of the workers' compensation payment process.

Our offices have worked together since the review's inception and, as a result, the CEO implemented or partially implemented 25 of the 26 recommendations. The CEO disagrees with one recommendation but proposed an alternative which, we believe, addresses the A-C's concern. The *Chief Executive Office Response to Auditor-Controller's Review of Workers' Compensation Payment Process* (Attachment I) provides specific comments concerning each recommendation.

We note the A-C's review and the CEO's responses determined that:

- No fraudulent activity was identified.
- The programming written to facilitate the interface between GenComp and eCAPS that caused duplicate payments was corrected.
- Split payments are nominal and third party administrator staff involved in the split payments were counseled or removed from the County's program.
- Within eight days of CEO staff receiving the list of seven payments believed to be undocumented, CEO staff located such documentation and so informed the A-C.
- GenComp/eCAPS interface issues are being resolved. The resolution of interface issues will expedite workers' compensation vendor payments and address a number of A-C concerns, including minimizing undeliverable payments and reducing the use of the "Hold File" and miscellaneous vendor codes.

Although the CEO concurs with many of the A-C's review recommendations and findings, the CEO provides comments that are grouped together utilizing your review's major sections (Attachment II).

The CEO will continue to work closely with your staff to fully implement these recommendations and strengthen the County's workers' compensation program. As agreed to in previous meetings with your staff, it is critical that the CEO receive significant technical assistance from A-C's eCAPS systems staff to resolve eCAPS interface issues described in the review and recommendations. We look forward to future collaboration in this area.

If you have any questions, please contact Rocky Armfield of my staff at (213) 351-5346.

DEJ:RAA
CA:DU:sg

Attachments

c: Sachi A. Hamai, Executive Officer, Board of Supervisors
    Maria Oms, Assistant Auditor-Controller
    Jim Schneiderman, Chief, Audit Division, Auditor-Controller
    Audit Committee

CHIEF EXECUTIVE OFFICE

RESPONSE TO AUDITOR-CONTROLLER'S REVIEW OF WORKERS' COMPENSATION PAYMENT PROCESS

NUMBER	RECOMMENDATION	STATUS	DEPARTMENT RESPONSE
1	Continue to work with Auditor-Controller (A-C) eCAPS personnel and complete a reconciliation of vendor information between GenComp and eCAPS.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. CEO began adding the GenComp vendor number to the vendor record in the eCAPS vendor table. In January 2006, CEO staff also implemented specialized matching "fuzzy logic" processes to improve the accuracy of the vendor matching process. CEO will continue to work with A-C eCAPS staff to reconcile vendor information between GenComp and eCAPS and to improve the accuracy of the reconciliation.
2	Perform an automated reconciliation of the information on GenComp with the eCAPS vendor file on a bimonthly basis.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. CEO is developing an automated vendor reconciliation process and will execute the process biweekly to ensure that additions and changes to the GenComp vendor table are interfaced to eCAPS timely and accurately.
3	Continue to work with the A-C to develop a method to ensure mismatches are corrected, and the information on GenComp and the eCAPS vendor tables are current and accurate so that payments are sent to the appropriate vendors' correct addresses.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. In June 2007, the CEO instituted strict, redundant controls for adding vendors to the eCAPS vendor table to verify that the vendors' addresses exist. In addition to these procedures, a "fuzzy logic" match is performed to ensure that the vendor record does not already exist in eCAPS. CEO will continue to work with A-C eCAPS staff to develop automated processes to validate vendor addresses, generate eCAPS address change transactions (VCMs), hold payment transactions until address changes are approved by the A-C, and continue to ensure payments are submitted using the appropriate eCAPS address codes.

NUMBER	RECOMMENDATION	STATUS	DEPARTMENT RESPONSE
4	Use automated procedures to detect vendors receiving payments under Miscellaneous Vendor Codes and add/update approved vendors to minimize the use of the Miscellaneous Vendor Codes.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. The A-C and CEO developed procedures to reduce workers' compensation payment delays to minimize the penalties that would be incurred on such delays. CEO management will continue to work with the A-C to implement additional measures to ensure that use of the Miscellaneous Vendor Codes is only when all requirements set forth by the A-C are met. Since July 2005, CEO documents all payments issued using a miscellaneous vendor code. CEO also mails letters and W-9 forms to vendors with a Taxpayer Identification Number (TIN)+Name mismatch on file. CEO will work with A-C eCAPS staff to develop a protocol for following up with vendors and for utilizing data elements on the eCAPS vendor table to denote the status of the mismatched information in order to minimize use of the Miscellaneous Vendor Code.
5	Review payments in the "Hold File" to correct mismatched addresses and add/update approved vendors to the eCAPS vendor file on a continuous basis.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. Since 2005, the CEO has been reviewing all payments in the "Hold File" on a daily basis to determine if the addresses have been updated on the eCAPS vendor table before transmitting the payments to eCAPS. CEO will continue to work with A-C eCAPS staff to better coordinate and schedule the submission and approval of batch additions, updates to the eCAPS vendor table, and add missing information/updates to eCAPS.
6	Develop and implement strict, redundant controls for adding vendors to GenComp modeling the controls used by the A-C to add vendors to the eCAPS vendor table, including comparing TINs to Internal Revenue Service (IRS) records and using address validation software to verify that the addresses exist.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. In June 2006, CEO instituted strict, redundant controls for adding vendors to the eCAPS vendor table to verify that the vendors' addresses exist. In addition, a "fuzzy logic" match is performed to ensure that the vendor record does not already exist in eCAPS.
7	Use automated procedures to review the GenComp vendor table to eliminate duplicate records and identify incomplete records for corrective action.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. Since vendor/biller records in GenComp cannot be deleted for historical reasons, the CEO plans to develop reports to identify duplicate or incomplete records so that CEO staff can manually review them and take the appropriate action to inactivate or correct.

NUMBER	RECOMMENDATION	STATUS	DEPARTMENT RESPONSE
8	Implement strict controls to deactivate and secure known bad addresses in GenComp to prevent them from being used, and deactivate the bad addresses in the eCAPS vendor table.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. Since 2006, all addresses from GenComp submitted to the eCAPS vendor table continue to be CASS (Coding Accuracy Support System)-certified, as required by the A-C. CEO will take appropriate action to deactivate incorrect addresses in GenComp, and will work with A-C staff to deactivate those addresses in eCAPS as well.
9	CAO management take action to increase its monitoring of TPAs and MMCs to ensure they comply with established payment control requirements.	Partially Implemented Target Date September 2007	CEO agrees with the recommendation. In January 2007, CEO staff met with TPA management to clarify and reiterate the long standing policy that payment requests cannot be split to circumvent established payment authority levels. In June 2007, CEO staff required County payment process controls be posted in the office of every TPA employee involved in the workers' compensation payment process. CEO staff and TPA management will implement random payment request audits to ensure compliance with payment control requirements.
10	CAO management evaluate the feasibility of lowering the threshold dollar amount so that more payments require a second approval and for requiring County monitor approvals.	Implement Alternate Option Target Date September 2007	CEO does not agree with the recommendation. However, as an alternate option, CEO staff and TPA management will implement random payment request audits to ensure compliance with payment control requirements. Since 2003, three of the four County workers' compensation claims administration units have been audited by the State of California, Division of Workers' Compensation Audit Unit. In each instance, the audited TPA met or exceeded the profile audit review performance standard and owed no administrative penalty for claims handling violations. Lowering the authorization threshold will increase the probability of payment transaction bottlenecks and expose the County to statutory and administrative penalties. CEO staff performs a fiscal reconciliation of all claim file indemnity payments upon receipt of an award or order issued by a workers' compensation judge. A recent analysis, shared with A-C staff, reflected 90 percent of all indemnity transactions and 89 percent of the total dollar amounts of all indemnity payments issued are evaluated during the reconciliation process.

NUMBER	RECOMMENDATION	STATUS	DEPARTMENT RESPONSE
11	Take immediate action to ensure that TPAs implement and maintain proper separation of duties and controls related to creating cases, authorizing payments, entering payment approvals, and changing payment information, such as address changes for service providers and injured workers.	Implemented	CEO agrees with the recommendation. In March 2007, procedures and controls, which were shared with the A-C, were implemented to maintain a proper separation of duties.
12	Immediately increase its monitoring of the TPAs' separation of duties to ensure the prescribed internal controls remain in force.	Implemented	CEO agrees with the recommendation. In June 2007, exception reports were developed by the CEO that will assist CEO staff and TPA management ensure that established internal controls are maintained.
13	Work with A-C staff to identify all duplicate payments caused by GenComp/eCAPS interface and take steps to recover the overpayments.	Partially Implemented Target Date July 2007	CEO agrees with the recommendation. In March 2006, the CEO immediately took corrective action measures to correct the GenComp/eCAPS interface programs for the specific cause identified. In a follow-up to this review, the A-C identified 28 possible duplicate payments totaling $11,000 occurring after March 2006. The CEO aggressively investigated the situation and believes the problem was caused by possible misinterpretation of manual procedures to cancel and reissue warrants. CEO has identified the status of all duplicate payments caused by the WC-eCAPS interface process. Once the A-C verifies that duplicate checks were cashed by providers, CEO will reflect such payments in GenComp and begin recovery efforts.
14	Identify and correct the GenComp/eCAPS interface system program errors that allow duplicate payments to be created.	Partially Implemented Target Date July 2007	CEO agrees with the recommendation. In March 2006, the CEO immediately took corrective action measures to correct the GenComp/eCAPS interface programs for the specific cause identified. In a follow-up to this review, the A-C identified 28 possible duplicate payments totaling $11,000 occurring after March 2006. The CEO aggressively investigated the situation and believes the problem was caused by possible misinterpretation of manual procedures to cancel and reissue warrants.

NUMBER	RECOMMENDATION	STATUS	DEPARTMENT RESPONSE
15	Develop and maintain documentation for the GenComp/eCAPS interface.	Implemented	CEO agrees with the recommendation. Efforts to fully document the WC-eCAPS interface began in January 2007 and were completed in June 2007.
16	Immediately stop the practice of backing up workers' compensation data on an unsecured, unencrypted hard drive, and limit off-site access, if necessary, to a secure connection, such as VPN.	Implemented	CEO agrees with the recommendation. In January 2006, after discovering that workers' compensation data was being backed up on unsecured devices, CEO took immediate action to stop the practice and re-educated staff on the importance of complying with CEO information security policies.
17	Separate the duties of system administrator, programmer, database administrator, and payment processor.	Implemented	CEO agrees with the recommendation. Since May 2007, the roles of application administration, programming, and database administration are separated functions between CEO Information Technology Service staff and GenComp staff.
18	Develop written policies to safeguard workers' compensation data.	Partially Implemented Target Date August 2007	CEO agrees with the recommendation. Written GenComp system data security policies exist as part of GenSource's support responsibilities, and CEO departmental data security policies are being updated.
19	CAO management modify GenComp automated access controls to address the weaknesses noted in our review.	Implemented	CEO agrees with the recommendation. In March 2007, the following automated access controls were incorporated as part of the GenComp upgrade/implementation: • User accounts are locked after a number of failed attempts. • User log-in attempts are recorded on the Citrix server. • User passwords expire every 45 days. • User passwords need to be at least six characters long, and must contain at least one letter in caps and one number. • Previously used passwords cannot be reused. • User accounts not logged in within 90 days are deactivated. • Users are timed out, both on Citrix and on the GenSource applications.

NUMBER	RECOMMENDATION	STATUS	DEPARTMENT RESPONSE
20	Develop monitoring reports to ensure that files are updated completely and accurately, and that unauthorized activities do not occur.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. GenComp: Monitoring reports and run-to-run controls exist for the GenComp application through the "GoodNite" process, and additional daily controls are administered by GenSource. WC-eCAPS Interface: Monitoring and control reports are being updated to ensure files are processed completely and accurately.
21	Develop written processing procedures for GenComp on how to review processing results to verify that processing was performed correctly.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. GenComp: Written procedures exist to review and verify GenComp processing results, including comprehensive "GoodNite" system assurance reports. WC-eCAPS Interface: Written processing procedures are being updated to ensure processing results are reviewed and verified.
22	Evaluate the feasibility of modifying GenComp to enable management to determine what transactions and activity were processed and to track changes made to individual transactions.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. GenComp: Management reports to review transaction activity exist for the GenComp application. WC-eCAPS Interface: Management reports are being refined to provide daily and monthly transaction activity summaries.
23	Evaluate the feasibility of incorporating edits, such as limits on the amounts and number of payments a payee can receive in a specified period, to reduce the risk of inappropriate transactions.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. CEO is working with GenSource to determine if such edits can be incorporated in the GenComp system. Since GenComp is a packaged and outsourced application, it may be that such controls would need to be developed outside of the application.

NUMBER	RECOMMENDATION	STATUS	DEPARTMENT RESPONSE
24	Develop and implement a formal change control policy for its computer applications.	Implemented	CEO agrees with the recommendation. GenComp is a fully-outsourced application supported by GenSource. All changes to GenComp are fully documented through an approved Work Order (Track) change control process. A monthly Open Track Report is produced to review outstanding tracks through analysis, development, test, and implementation. In June 2007, the CEO also instituted a formal change control process for the WC-eCAPS interface process. All system modifications must be reviewed and approved by CEO's Information Technology Service manager and all functional enhancements must also be signed off by CEO's Risk Management Branch and Budget and Fiscal Services.
25	Develop and test a Business Continuity Plan for GenComp.	Partially Implemented Target Date October 2007	CEO agrees with the recommendation. GenComp: GenComp is a fully-outsourced application supported by GenSource. A complete Disaster Recovery Plan (DRP) is in place for the system. WC-eCAPS Interface: A DRP plan for the WC-eCAPS interface will be developed by CEO Information Technology Service staff.
26	CAO management ensure that the annual Internal Control Certification Program (ICCP) review of the GenComp system is conducted accurately and by someone independent of the system operations/administration.	Implemented	CEO agrees with the recommendation. In May 2007, CEO completed the first annual independent ICCP review of the GenComp system, which included the WC-eCAPS interface process.

WC audit response chart 07-03-07

CHIEF EXECUTIVE OFFICE
Auditor-Controller's Review of Workers' Compensation Payment Process

Summary of Responses

Background

The Chief Executive Office (CEO) operates and administers the County of Los Angeles' (County) self-insured workers' compensation program. Workers' compensation claim administration services are performed by third party administrators (TPAs). CEO and TPA management have developed professional relationships to continually strengthen the County's workers' compensation program. These relationships also facilitated the implementation of a number of the A-C's recommendations found in the review. Program enhancements and legislative reforms resulted in cost avoidance of approximately $250 million in Fiscal Year 2006-07.

Chief Executive Officer Summary

The "Workers' Compensation Payments" section of the A-C's review (Page 1) includes comments and findings related to undeliverable payments due to mismatches between the GenComp and eCAPS vendor tables. When mismatches occur, to avoid workers' compensation penalties if a payment is untimely, the CEO created a "Hold File" and Miscellaneous Vendor Codes (MVCs) to process vendor payments.

To address the issues included in the A-C's review, which in great part involve "growing pains" that accompany the implementation of new systems like eCAPS, the CEO provides the following clarifications/response:

- Prior to July 1, 2005, all County workers' compensation payments were paid using MVCs. When eCAPS was implemented in July 2005, the GenComp vendor information was converted into the eCAPS vendor table; and, for the first time, new interfaces were required between GenComp and eCAPS to submit payments and vendor updates from GenComp to eCAPS. In July 2005, many of the current procedures and practices related to vendor controls were not yet established by the A-C, and some existing procedures were updated after eCAPS' implementation to improve controls. Accordingly, over the last two years, A-C and CEO staff worked together to enhance or implement automated and manual procedures to comply with the new eCAPS controls. A-C staff worked to develop detailed procedures for automated interfaces, and CEO staff researched and implemented specialized matching logic for the process.

- Since July 2005, the new eCAPS controls applicable to vendor updates included processes for eCAPS vendor matching, Internal Revenue Service-Taxpayer Identification Number (TIN) verification, TIN-name matching, address verification, and W-9 distribution and confirmation. Prior to July 2005, such processes were not CEO functions. The CEO has discussed with the A-C whether these functions would be better processed by the A-C or contractors possessing the necessary expertise. The complexity and size of the workers' compensation program compounds the problem.

- The CEO initiated a payment "Hold File" to provide time to resolve individual vendor issues before transmitting the payments from GenComp to eCAPS, and to minimize the number of rejected payment transactions in the eCAPS document catalog. The CEO, with guidance from A-C, made enhancements to the process of resolving vendor issues and improving the efficiency of the automated vendor updates.

- The "Hold File" must remain an integral part of the GenComp to eCAPS interface. Its continued use is critical to ensure timely and accurate payment transactions. The CEO will continue to work with A-C staff to enhance the efficiency of the automated and manual interface processes and minimize the use of MVCs.

The "TPA Payment Controls" section of the review (Page 5) discusses the TPA procedures and practices utilized to make workers' compensation payments. The CEO provides the following response:

- On April 4, 2007, at the request of CEO staff, A-C staff provided a consolidated list of "payments in excess of approved amounts." CEO staff investigated the $4,032 overpayment addressed in the A-C's review (Page 6) and determined the overpayment resulted from payments issued to comply with an interim court order arising from a claimant's death. Additionally, CEO staff verified the $4,032 addressed was recovered. Any potential remaining overpayment will be recovered at the time of final settlement as outlined in the interim court order. This information was provided to A-C staff on April 16, 2007.

- On April 20, 2007, at the request of CEO staff, A-C staff provided a consolidated list of the seven payments found to have "no documentation that the invoices had been approved by TPA and MMC staff." CEO staff verified documentation existed to support the seven payments addressed on page six of your review. The invoices were approved by the TPA and processed by the County's medical and disability management contractor. On April 28, 2007, CEO staff's findings were shared with A-C staff. CEO staff offered to provide supporting documentation to the A-C.

- The TPA's delegation of authority noted on page six of your review is an accepted insurance industry practice and complies with payment processing procedures.

- CEO staff investigated the ten payments reported (Page 6) as appearing to be split. CEO staff determined each payment comported to appropriate workers' compensation benefits owed; and no evidence of fraud, duplicate payment, overpayment, or excess cost was found. The CEO does not allow unauthorized split payments. The CEO requires TPA management to counsel first-time offenders and remove examiners found to have split payments to circumvent authority levels.

- Since January 1, 2001, the CEO's extensive on-site monitoring of the workers' compensation TPA contracts has resulted in required reimbursements from the TPAs to the County of more than $9.25 million. However, CEO and TPA management have maintained professional relationships to ensure successful implementation of the 2003 and 2004 workers' compensation reforms, enhancements to the County's workers' compensation program, and additional fiscal monitoring of workers' compensation payment processes.